longer of five years from such date and the current term of such agreement; and (ii) certain existing facilities agreements, facilities lease agreements or other arrangements (including arrangements relating to future agreements) relating to the lease or other grant of right to use fiber optic facilities between such Cable Stockholder or any of its affiliates and TCG or any of its subsidiaries would be automatically amended as of January 8, 1998 to conform with a form of Master Facilities Agreement agreed to by AT&T, the Cable Stockholders and TCG at the time of the execution of the AT&T Agreement.

Consummation of the AT&T Merger is subject to certain closing conditions, including TCG and AT&T obtaining certain required regulatory approvals and other related consents. Accordingly, there can be no assurance that the AT&T Merger will be successfully consummated or, if successfully completed, when it might be completed.

THE ACC MERGER

On November 26, 1997, TCG entered into an Agreement and Plan of Merger (the "ACC Agreement") by and among TCG, TCG Merger Co., Inc., a Delaware corporation and a wholly-owned subsidiary of TCG ("MergerCo"), and ACC Corp., a Delaware corporation ("ACC"), providing for the merger of MergerCo with and into ACC (the "ACC Merger"), with ACC becoming a wholly-owned subsidiary of TCG. ACC is a switch-based provider of telecommunications services to businesses, residential customers, and educational institutions in the United States, United Kingdom and Canada. ACC has recently commenced operations in Germany. The ACC Agreement provides that ACC's stockholders will receive approximately that number of shares of TCG Class A Common Stock for each ACC share, equal to $50 divided by the average per share closing price of TCG Class A Common Stock for a ten-day trading period prior to closing of the transaction. In the event, however, that the average per share closing price of TCG Class A Common Stock during such ten-day trading period prior to closing is below $45, the exchange ratio is fixed at 1.11111 shares of TCG Class A Common Stock for each ACC share, and, if the average per share closing price of TCG Class A Common Stock during such ten-day trading period prior to closing is above $55, the exchange ratio is fixed at 0.90909 of a share of TCG Class A Common Stock for each ACC share. The total aggregate amount of consideration to be received by the ACC stockholders is expected to be approximately $1 billion. Statements made herein regarding the ACC Agreement are not complete, and reference is made to the copy of the ACC Agreement filed with the Commission as an exhibit to TCG's Registration Statement on Form S-4 (File No. 333-45833) (the "ACC S-4").

TCG and ACC expect the transaction to be completed by the end of the second quarter of 1998, subject to, among other things, approval by a majority of the holders of ACC's outstanding shares. Under the ACC Agreement, ACC has agreed not to solicit or take other actions with respect to any competing proposal, subject to compliance with fiduciary duties. ACC agreed to pay TCG $32.5 million, plus up to $7.5 million for expenses, if the ACC Agreement is terminated under certain circumstances.

Upon execution of the ACC Agreement, ACC amended its shareholder rights plan to exempt TCG from the 7.5% threshold by which the rights become exercisable. This amendment will remain in effect until December 31, 1998. In the event that the ACC Merger is completed, the underlying rights granted under the ACC shareholder rights plan will be redeemed by ACC.

Consummation of the ACC Merger is subject to certain closing conditions, including TCG and ACC obtaining required regulatory approvals and other related consents. Accordingly, there can be no assurance that the ACC Merger will be successfully consummated or, if successfully completed, when it might be completed.

OTHER RECENT DEVELOPMENTS

Kansas City Fiber Network, L.P. In December 1997, TCG agreed to purchase substantially all of the assets used in connection with a fiber optic communications system of Kansas City Fiber Network, L.P., a CLEC, a majority of the equity of which is owned by TCI. Pending the closing of such transaction, TCG is providing certain services in connection with the operations of such communications system, which is located in the Kansas

- *Capitalize on management team experience.* TCG's management team is comprised of executives who are recognized as leaders in the development of the competitive local telecommunications industry. This management team has extensive operational, technical, financial and regulatory expertise as well as a proven track record in a rapidly changing marketplace.

The AT&T Agreement (as defined below) contains certain restrictions on the conduct of TCG's business prior to the consummation of the AT&T Merger which are likely to affect TCG's pursuit of its strategies.

THE TCG REORGANIZATION

In June 1996, TCG and the Cable Stockholders completed the consolidation of the ownership of TCG Partners (a New York general partnership which was initially owned by the Cable Stockholders in the same percentages as TCG) and of 14 local market partnerships (the "Local Market Partnerships") as wholly-owned subsidiaries of TCG (the "TCG Reorganization").

THE AT&T MERGER

On January 8, 1998, TCG entered into an Agreement and Plan of Merger (the "AT&T Agreement") with AT&T Corp., a New York corporation ("AT&T"), and TA Merger Corp., a Delaware corporation and a wholly-owned subsidiary of AT&T ("AT&T Merger Sub"), pursuant to which, subject to satisfaction of the closing conditions specified therein, AT&T Merger Sub would merge with and into TCG, with TCG surviving as a wholly-owned subsidiary of AT&T (the "AT&T Merger"). TCG and AT&T expect that the AT&T Merger will be consummated subsequent to the consummation of the ACC Merger (as defined below). Statements made herein regarding the AT&T Agreement are not complete, and reference is made to the copy of the AT&T Agreement filed with the Commission as an exhibit to TCG's Report on Form 8-K, on January 26, 1998. The following disclosure is qualified in its entirety by such reference.

In the AT&T Merger, each share of TCG Class A Common Stock (including shares issued to former ACC stockholders in the ACC Merger, assuming that the ACC Merger occurs prior to the AT&T Merger) and each share of the Class B Common Stock of TCG, par value $0.01 per share (the "TCG Class B Common Stock," and, together with the TCG Class A Common Stock, the "TCG Common Stock") will be converted into 0.943 of a share of AT&T common stock. TCG and AT&T expect that the exchange will be tax-free to TCG stockholders, except to the extent cash is received in lieu of fractional shares. The AT&T Agreement contains customary representations and warranties of the parties, which will not survive effectiveness of the AT&T Merger. In addition, the AT&T Agreement contains certain restrictions on the conduct of TCG's business prior to the consummation of the AT&T Merger. Pursuant to the AT&T Agreement, TCG has agreed, for the period prior to the AT&T Merger, to operate its business in the ordinary course, to refrain from taking various corporate actions without the consent of AT&T, and not to solicit or enter into negotiations or agreements relating to a competing business combination.

Pursuant to a Voting Agreement among the Cable Stockholders and AT&T, each Cable Stockholder executed and delivered to TCG a written consent in favor of and approving the AT&T Agreement and the AT&T Merger. As a result, so long as the AT&T Agreement is not amended and no provision of it is waived, no further vote or meeting of TCG stockholders is necessary to approve or consummate the AT&T Merger. AT&T will register the shares of AT&T common stock to be issued in the AT&T Merger in exchange for shares of TCG Common Stock. AT&T will file a Registration Statement on Form S-4 to register such shares of AT&T Common Stock, and such registration statement will contain an information statement that TCG will distribute to its stockholders.

Pursuant to the Voting Agreement, each of the Cable Stockholders, on behalf of itself and certain of its affiliates, also agreed that (i) certain right-of-way, colocation and similar agreements with TCG and its affiliates would be amended as of January 8, 1998 to provide that each such agreement would remain in effect for the available packaged with TCG's already comprehensive offerings of local services. TCG leverages its existing network investment by routing and switching as great a portion of long distance services as possible over its existing local and regional facilities, with the balance of such services being provided by the resale of the services of other carriers. For example, TCG has substantially completed a reconfiguration of the many adjacent local networks it operates between Boston and Washington, D.C. into a regional network covering a geographic area extending from southern New Hampshire to northern Virginia.

- *Expand geographic reach and density of existing networks and enter new markets.* In response to customer demand, the Company continues to increase the geographic reach and density of its existing networks by deploying additional fiber optic rings and connecting additional customers to its networks. The Company anticipates that making significant capital expenditures over the next several years to expand its existing networks and to develop new networks will lead to significant increases in revenue opportunities. The Company may also make selected acquisitions. As a facilities-based carrier, the Company utilizes a variety of means to expand geographically, including rights-of-way, easements, poles, ducts and conduits that are available from cable television operators, ILECs, railways, subways, electric, gas and water utilities and municipal, state and federal street and highway authorities. In the course of expanding its networks, TCG also has the ability to reach TCG customers by reselling all or a portion of the telecommunications services offered by ILECs. However, TCG believes that the extensive geographic reach and density of its networks make it less reliant than other CLECs on the networks of the ILECs. In addition, where appropriate, the Company has the ability to link its customers to its networks through a variety of technologies including the use of microwave services, including 38 gigahertz ("GHz") milliwave services. TCG plans to expand into additional metropolitan markets, which TCG believes will further broaden its customer base and enhance its ability to attract national business accounts for its services.
- *Offer high quality networks and superior customer service.* TCG believes that it offers cost and service quality advantages over ILECs as a result of its integrated operations, customer support, network monitoring and management systems and state-of-the-art technology deployed in TCG's digital networks. TCG consults closely with its customers to develop competitively priced telecommunications services that are tailored to their particular needs. TCG's centrally managed customer care and support operations are also designed to facilitate the processing of orders for changes and upgrades in services. TCG believes that it provides greater attention and responsiveness to its customers than do the ILECs.
- *Benefit from working relationships with cable television operators.* As of December 31, 1997, the cable television facilities of TCI, Cox and Comcast collectively passed approximately 38% of the country's 94.5 million homes passed by cable television facilities. Through its relationships with cable television operators, including the Cable Stockholders, TCG has historically been able to utilize existing rights-of-way, obtain fiber optic facilities and share the cost of building new fiber optic networks, thereby allowing TCG to achieve significant economies of scale and scope through capital efficiencies in extending its existing networks in a rapid, efficient and cost-effective manner. TCG is currently working with certain Cable Stockholders for the provisioning of residential or multiple dwelling unit telephony services with TCG providing switching, call processing, calling features and ancillary services. Beginning as technical trials, these efforts have expanded into limited commercial offerings in certain locations in Connecticut, Michigan, California, Illinois, Maryland, Texas and Florida.
- *Spearhead regulatory reform.* As the first and largest CLEC, TCG has been at the forefront of industry efforts for over a decade to introduce competition to the local telecommunications market. TCG has aggressively pursued the goal of making competitive local exchange services economically, technically and operationally feasible by working for legislative and regulatory reform and through negotiations with ILECs. TCG has continued its regulatory reform activities in an effort to ensure that the 1996 Act is implemented and interpreted in a manner that promotes fair competition for telecommunications services.

TCG has historically benefited from its relationships with the parents of its Class B stockholders. TCI Communications, Inc. (together with its consolidated subsidiaries, "TCI"), Cox Communications, Inc. (together with its consolidated subsidiaries, "Cox"), Comcast Corporation (together with its consolidated subsidiaries, "Comcast") and, for periods prior to November 13, 1997, MediaOne of Delaware, Inc., formerly Continental Cablevision, Inc. (together with its consolidated subsidiaries, "Continental") (collectively, the "Cable Stockholders"), which are among the largest cable television companies in the United States. Through such relationships, the Company has been able to utilize rights-of-way, obtain fiber optic facilities and share the cost of building new fiber optic networks, thereby allowing TCG to achieve significant economies of scale and scope through capital efficiencies in extending its networks in a rapid, efficient and cost-effective manner.

The Company believes that it has several advantages that enable it to compete successfully in the new competitive telecommunications marketplace, including (i) extensive, technologically advanced networks located or under development in major metropolitan markets nationwide, (ii) state-of-the-art information systems, (iii) an experienced management team with significant operational, technical, financial and regulatory expertise in the telecommunications industry, (iv) positive relationships with its broad array of commercial customers, (v) TCG's reputation for high quality service, and (vi) established relationships with cable television operators.

BUSINESS STRATEGY

As a premier competitive local telecommunications carrier, the key elements of the Company's business strategy are to:

- *Provide a wide range of local telecommunications services.* The Company provides a broad array of telecommunications services to meet the voice, data and video transmission needs of its customers, including basic local exchange telephone services, enhanced switched services, dedicated services, high speed switched data services, Internet services, disaster avoidance services and video channel transmission services. Switched services revenue increased 90% for the year ended December 31, 1997 from the switched services revenue for the year ended December 31, 1996 on a pro forma basis. In 1997, approximately 44% of TCG's revenues were generated from switched services. TCG expects a growing portion of its revenue to be derived from basic local exchange telephone services, enhanced switched services, Internet services and high speed switched data services as it continues to deploy digital switches in its markets.
- *Focus on business customers and telecommunications carriers.* The Company's networks serve large metropolitan markets, which have significant concentrations of telecommunications-intensive businesses. The Company's customers in these markets include financial services companies, media and insurance companies, long distance carriers and resellers, healthcare and educational institutions, governmental agencies, Internet service providers, disaster recovery service providers, wireless communications companies, residential multiple dwelling units and an increasing number of small and medium-sized business customers. The national scope of TCG's local networks allows it to offer high volume business customers and long distance carriers uniformity of services, pricing, quality standards and customer service. In addition, TCG has arrangements with other telecommunications providers, including shared tenant services providers, cable television companies and long distance carriers, to resell TCG's services. In 1997, approximately 66% of TCG's revenues were generated from business customers (including resellers) and approximately 34% were generated from long distance carrier customers.
- *Offer local and long distance services.* TCG believes there is a growing demand, especially from small to medium-sized businesses, for telecommunications carriers to offer comprehensive packages of services so that a customer may obtain most or all of its telecommunications needs from a single provider. In September 1997 TCG broadened its existing long distance products into a general offering of long distance services in 22 metropolitan areas. These services have enhanced features and are

PART I

Item 1. *Business*

INTRODUCTION

Teleport Communications Group Inc. (the "Company" or "TCG" or the "Registrant") is the first and largest competitive local exchange carrier ("CLEC") in the United States and offers comprehensive telecommunications services in major metropolitan markets nationwide. TCG competes with incumbent local exchange carriers ("ILECs") by providing high quality, integrated telecommunications services, primarily over fiber optic digital networks, to meet the voice, data and video transmission needs of its customers. TCG's customers are principally telecommunications-intensive businesses, healthcare and educational institutions, governmental agencies, long distance carriers and resellers, Internet service providers, disaster recovery service providers, wireless communications companies and financial services companies. TCG offers these customers technologically advanced telecommunications services, as well as superior customer service, flexible pricing and vendor and route diversity. TCG was incorporated in 1983 under the laws of the State of Delaware.

For over 13 years, TCG has developed, operated and expanded its local telecommunications networks. During the fourth quarter, TCG added eight new markets, which brings total Metropolitan Statistical Areas ("MSAs") served by TCG to 65. These 65 MSAs were located in metropolitan New York/New Jersey, Los Angeles, Chicago, San Francisco, Philadelphia, Boston, Detroit, Baltimore, Washington, D.C., Dallas, Houston, Miami/Ft. Lauderdale, Seattle, San Diego, St. Louis, Pittsburgh, Phoenix, Denver, Milwaukee, Indianapolis, Hartford, Omaha, Providence, Cleveland, Portland (Oregon), Salt Lake City, Nashville, Chattanooga, Knoxville, Birmingham, Cincinnati, Columbus (Ohio), Charlotte, Tampa Bay, Sacramento, Minneapolis-St. Paul, Atlanta and Orlando, including 19 of the 20 largest metropolitan areas. As of December 31, 1997, TCG's fiber optic networks spanned over 9,470 route miles, contained over 491,090 fiber miles and served approximately 13,510 buildings.

TCG has grown rapidly over the last several years, expanding its existing networks, developing new networks and increasing its service offerings. For 1997, the Company's revenues were $494.3 million, an increase of $210.9 million or 74% over its revenues on a pro forma basis for 1996. Substantially all of this growth was derived from the provision of local telecommunications services.

Total revenues from the local telecommunications market in the United States were estimated to have been approximately $104 billion in 1997. In the past, competitive access providers, including TCG, were limited to serving only the dedicated services portion of this market, which was estimated to have been approximately $6 billion in 1997, whereas the local switched services portion of this market for business customers was estimated to have been approximately $62 billion. TCG has been expanding into the switched services market over the last nine years by constructing switched networks and obtaining the necessary regulatory authorizations and interconnection arrangements to become a CLEC.

TCG believes that it is well positioned with the passage and initial implementation of the Telecommunications Act of 1996 (the "1996 Act") to address a significantly larger portion of the telecommunications market and to improve its operating margins in the switched and dedicated services markets by expanding its networks, installing additional high capacity digital switches (as well as increasing the switching capacity of existing switches) and offering new products and services. Also, in 1996, TCG introduced a new service offering consisting of basic Internet access for business customers, and in February 1997, TCG acquired CERFnet Services, Inc. ("CERFnet"), a leading regional Internet service provider ("ISP") for business customers. See "Business—Other Recent Developments." As of December 31, 1997, TCG offered a variety of Internet services in 22 metropolitan areas.

In September 1997, TCG introduced a general long distance service offering packaged with its existing local services in 22 metropolitan areas. The service is being provided primarily through the resale of other carriers' services, although TCG provides long distance services over its own facilities wherever possible.

TABLE OF CONTENTS

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-K

(Mark One)

☒ Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 1997

or

☐ Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from to

Commission file number 0-20913

Teleport Communications Group Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**13-3173139**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
437 Ridge Road, Executive Building 3, Dayton, NJ	**08810**
(Address of Principal Executive Offices)	**(Zip Code)**

732-392-2000

(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
None	None

Securities registered pursuant to Section 12(g) of the Act:

Class A Common Stock

(Title of Class)

Indicate by check mark whether the Registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

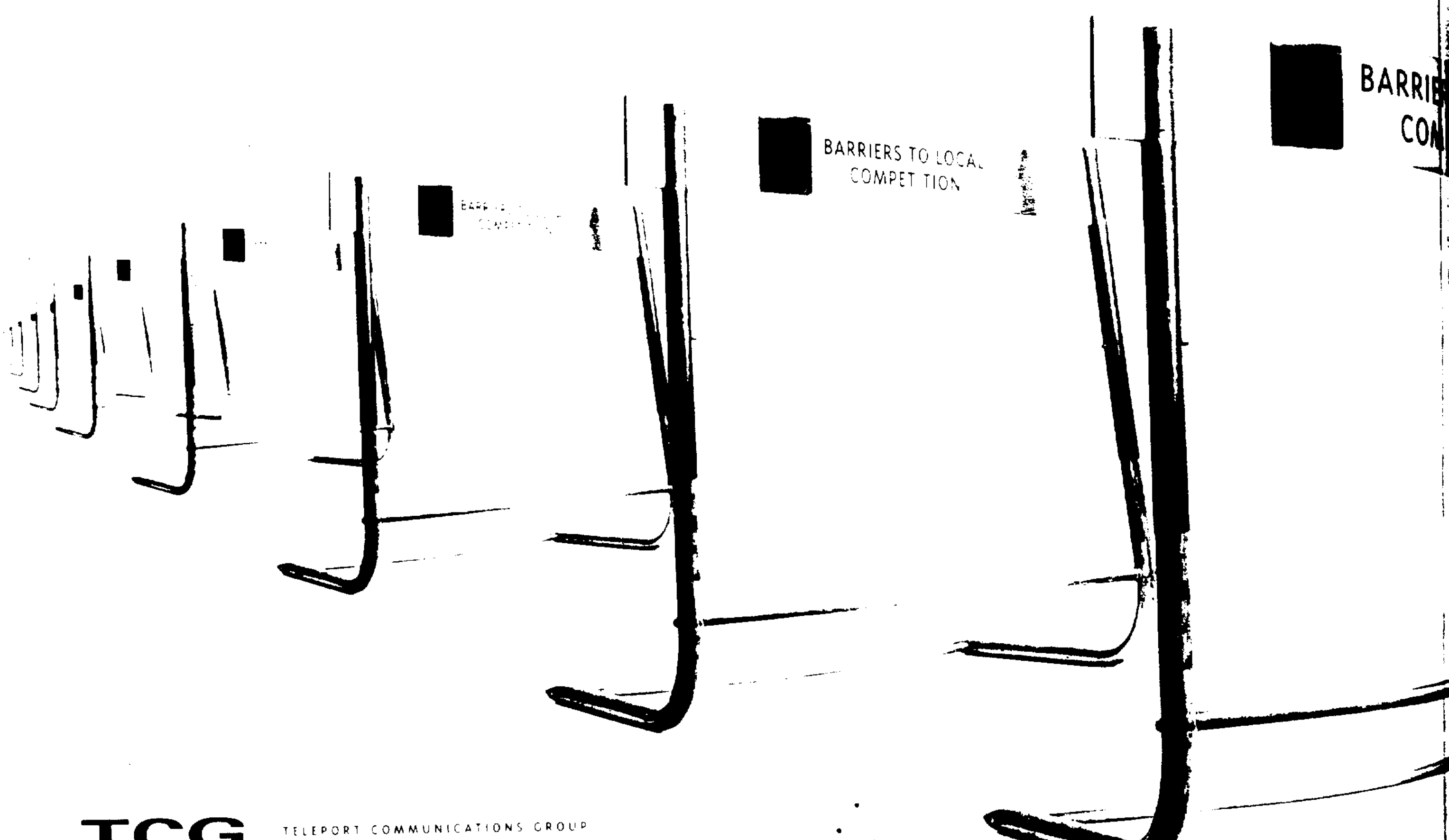
Based on the closing sales price on March 5, 1998 the aggregate market value of the voting and non-voting stock held by non-affiliates of the Registrant was approximately $2,638,426,380.

At March 5, 1998, 61,502,790 shares of the Registrant's Class A Common Stock and 113,489,040 shares of Registrant's Class B Common Stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement to be filed with the Securities and Exchange Commission in connection with its 1998 Annual Meeting are incorporated by reference into Part III of this Report on Form 10-K.

Certain portions of the Registrant's Registration Statement on Form S-3 (File No. 333-37597) are incorporated by reference in this Report on Form 10-K.



TCG

TELEPORT COMMUNICATIONS GROUP

Two Teleport Drive • Staten Island, NY 10311-1011 • 718 355 2000 • http://www.tcg.com

BOARD OF DIRECTORS

Robert Annunziata
Chairman, President and Chief Executive Officer
Teleport Communications Group Inc.

Gary S. Howard
President and Chief Executive Officer
TCI Ventures Group, LLC

John R. Dillon
Managing Director
Cravey, Green & Whalen Inc.

Gerald W. Gaines
Senior Vice President
TCI Communications, Inc.

Jimmy W. Hayes
Senior Vice President
Cox Communications, Inc.

J. Bruce Llewellyn
Chairman
The Philadelphia Coca-Cola Bottling Company

James O. Robbins
President and Chief Executive Officer
Cox Communications, Inc.

John R. Alchin
Senior Vice President and Treasurer
Comcast Corporation

C.B. (Jack) Rogers
Chairman
Equifax Inc.

Larry Romrell
Executive Vice President
Tele-Communications, Inc.

Bernard (Barney) W. Schotters
Senior Vice President
Tele-Communications, Inc.

Lawrence S. Smith
Executive Vice President
Comcast Corporation

David M. Woodrow
Senior Vice President
Cox Communications, Inc.

STOCKHOLDER REFERENCE INFORMATION

Transfer Agent

Inquiries by stockholders about stock transfers, address changes, etc., should be directed to:
The Bank of New York
Shareholders Relations Dept.-11E
P.O. Box 11258
Church Street Station
New York, NY 10286
Tel 800.524.4458
E-mail Shareowner-svcs@bankofny.com

Investor Relations

Inquiries by security analysts, investment professionals and stockholders about TCG common stock, including requests for SEC or other stockholder reports, should be directed to:
Vice President, Investor Relations
Teleport Communications Group
Princeton Technology Center
429 Ridge Road
Dayton, NJ 08810-1014
Tel 732.392.2154
Fax 732.392.3740
Internet Address:
http://www.tcg.com

Common Stock

Teleport Communications Group Inc. Class A Common Stock is traded on the NASDAQ National Market under the symbol: TCGI

Annual Meeting of Stockholders

The annual meeting of stockholders will be held on May 13, 1998 at The Villas of Grand Cypress in Orlando, Fla.

Form 10-K

After the close of each fiscal year, TCG submits a report on Form 10-K to the Securities and Exchange Commission containing certain additional information about its business. A copy of this report may be obtained without charge by contacting Investor Relations.

Auditors

Deloitte & Touche LLP
New York, NY

Price Range of Common Stock

The following tables provide the high, low and closing sale price as well as the volume of the common stock for the four quarters of 1997 and the last three quarters of 1996.

TCG Market Price and Volume of Shares Traded

As of March 23, 1998, there were approximately 12,453 shareholders of record.

1997	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
High	35.250	34.125	46.125	60.219
Low	22.625	21.000	33.500	44.250
Close	23.000	34.125	44.875	54.875
Volume	17 million shares	21 million shares	28 million shares	94 million shares

1996	Second Quarter	Third Quarter	Fourth Quarter
High	19.125	27.375	35.375
Low	16.000	14.125	22.000
Close	19.125	23.625	30.500
Volume	15 million shares	39 million shares	19 million shares

Dividend Policy

TCG has not paid any cash dividends on its common stock. The company intends to retain future earnings, if any, to finance the development and expansion of its businesses and, therefore does not anticipate paying dividends. Any dividends will be made by the Board of Directors in light of conditions then existing, including TCG's results of operations, financial condition and requirements, business conditions and other factors.

[illegible] report were printed on recycled paper

PBX trunk • A transmission facility which connects a PBX to a CLEC's or ILEC's central office switching center.

POPs (Points Of Presence) • Locations where a long distance carrier has installed transmission equipment in a service area that serves as, or relays telephone calls to, a network switching center of the same long distance carrier.

Peering arrangements • Arrangements between Internet service providers which allow them to establish mutual connections to the Internet on a preferred basis.

Private line • A private, dedicated telecommunications link between different customer locations (excluding long distance carrier POPs).

Public switched network • The switched network available to all users generally on a shared basis (i.e., not dedicated to a particular user). The local exchange telephone service networks operated by ILECs are the largest and often the only public switched networks in a given locality.

PUC (Public Utility Commission) or State PUC • A state regulatory body, established in most states, which regulates utilities, including telecommunications companies providing intrastate services. In some states this regulatory body may have a different name, such as public service commission ("PSC").

RBOC (Regional Bell Operating Company) • The holding company which owns a BOC.

Reciprocal compensation • An arrangement in which two local exchange carriers agree to terminate traffic originating on each other's networks in exchange for a negotiated level of compensation.

Route mile • The number of miles along which fiber optic cables are installed.

SONET (Synchronous Optical Network) • A set of standards for optical communications transmission systems that define the optical rates and formats, signal characteristics, performance, management and maintenance information to be embedded within the signals and the multiplexing techniques to be employed in optical communications transmission systems. SONET facilitates the interoperability of dissimilar vendor equipment. SONET benefits business customers by minimizing the equipment necessary for various telecommunications applications and supports networking diagnostic and maintenance features.

Special access services • The lease of private, dedicated telecommunications lines or circuits on an ILEC's or a CLEC's network which run to or from the long distance carrier's POPs. Special access services do not require the use of switches. Examples of special access services are telecommunications circuits running between POPs of a single long distance carrier, from one long distance carrier's POP to another long distance carrier's POP or from an end user to its long distance carrier's POP.

Switch • A mechanical or electronic device that opens or closes circuits or selects the paths or circuits to be used for the transmission of information. Switching is a process of linking different circuits to create a temporary transmission path between users. Within this document, switches generally refer to voice grade telecommunications switches unless specifically stated otherwise.

Switched access services • The connection between a long distance carrier's POP and an end user's premises through the switching facilities of a local exchange carrier.

Toll services • Otherwise known as Extended Area Service, EAS or intraLATA toll services are those calls that are beyond the free local calling area but originate and terminate within the same LATA, such calls are usually priced on a measured basis.

Tier I Internet service provider • An Internet service provider which has peering arrangements with other leading Internet service providers.

Voice grade equivalent circuit • One DS-0. One voice grade equivalent circuit is equal to 64 kilobits of bandwidth.

Hybrid Fiber Coaxial (HFC) • A technology consisting of fiber optic distribution facilities and coaxial cable deployed to the home or business. This technology enables the operator to offer a wide variety of two-way broadband services, including telecommunications and entertainment.

ILECs (Incumbent Local Exchange Carriers) • The local phone companies, either a BOC or an independent carrier (such as GTE) which provides local exchange services.

Internet • The name used to describe the global open network of computers that permits a person with access to the Internet to exchange information with any other computer connected to the network.

ISDN (Integrated Services Digital Network) • ISDN is an internationally agreed standard which, through special equipment, allows two-way, simultaneous voice and data transmission in digital formats over the same transmission line. ISDN permits video conferencing over a single line, for example, and also supports a multitude of value-added switched service applications such as Incoming Calling Line Identification. ISDN's combined voice and data networking capabilities reduce costs for end users and result in more efficient use of available facilities. ISDN combines standards for highly flexible customer to network signaling with both voice and data within a common facility.

ISP • Internet service provider.

IXC (Interexchange Carrier) • A long distance carrier.

Kbps (kilobits) • One thousand bits of information. The information-carrying capacity (i.e., bandwidth) of a circuit may be measured in "thousands of bits per second."

LANs (Local Area Networks) • The interconnection of computers for the purpose of sharing files, programs and peripheral devices such as printers and high-speed modems. LANs may include dedicated computers or file servers that provide a centralized source of shared files and programs. LANs are generally confined to a single customer's premises and may be extended or interconnected to other locations through the use of bridges and routers.

LATA (Local Access and Transport Area) • The geographical areas within which a local telephone company may offer telecommunications services, as defined in the divestiture order known as the Modified Final Judgment ("MFJ") unless and until redefined by the FCC pursuant to the Telecommunications Act of 1996.

Local Exchange • A geographic area defined by the appropriate state regulatory authority in which telephone calls generally are transmitted without toll charges to the calling or called party.

Local Exchange Service/Local Exchange Telephone Service • Basic local telephone service, including the provision of telephone numbers, dial tone and calling within the local exchange area.

Long Distance Carriers (Interexchange Carriers or IXCs) • Long distance carriers providing services between LATAs, on an interstate or intrastate basis. A long distance carrier may be facilities-based or offer service by reselling the services of a facilities-based carrier.

Local Transport Services • Dedicated lines between the ILEC's central offices and long distance carrier POPs used to carry switched traffic.

Mbps (Megabits) • One million bits of information. The information-carrying capacity (i.e., bandwidth) of a circuit may be measured in "millions of bits per second."

Multiplexing • An electronic or optical process that combines a number of lower speed transmission signals into one higher speed signal. There are various techniques for multiplexing, including frequency division (splitting the total available frequency bandwidth into smaller frequency slices), time division (slicing a channel into time slots and placing each signal into its assigned time slot), and statistical (wherein multiplexed signals share the same channel and each transmits only when it has data to send).

Nodes • An individual point of origination and termination or intersection on the network, usually where electronics are housed.

PBX (Private Branch Exchange) • A customer owned and operated switch on customer premises, typically used by large businesses with multiple telephone lines.

Access charges • The fees paid by long distance carriers for the local connections between the long distance carriers' networks and the long distance carriers' customers.

ATM (Asynchronous Transfer Mode) • A commercialized switching and transmission technology that is one of a general class of packet technologies that relay traffic by way of an address contained within the first five bits of a standard fifty-three bit-long packet or cell. ATM-based packet transport was specifically developed to allow switching and transmission of mixed voice, data and video at varying rates. The ATM format can be used by many different information systems, including LANs.

BOC (Bell Operating Company) • A telephone operating subsidiary of an RBOC; an incumbent local exchange carrier.

Central offices • A telecommunications center where switches and other telecommunications facilities are housed. CLEC's may connect with ILEC networks either at this location or through a remote location.

Centrex • A switched service that offers dial tone and other features similar to those of Private Branch Exchange ("PBX"), except the switching equipment is located at the carrier's premises and not at the customer's premises. These features include direct dialing within a given telephone system, direct dialing of outgoing telephone calls and automatic identification of incoming telephone calls. This is a value-added service that carriers can provide to a wide range of business customers.

Colocation • The ability of a telecommunications carrier to interconnect its network to the ILEC's network by extending its facilities to the ILEC's central office. Physical colocation occurs when the interconnecting carrier places its network equipment within the ILEC's central offices. Virtual colocation is an alternative to physical colocation under which the ILEC permits a carrier to interconnect its network to the ILEC's network in a manner which is technically, operationally and economically comparable to physical colocation, even though the interconnecting carrier's network connection equipment is not physically located within the central offices.

CLEC (Competitive Local Exchange Carrier) • A company that provides local exchange services in competition with the incumbent local exchange carrier.

Dedicated • Telecommunications lines dedicated to, or reserved for use by, a particular customer along predetermined routes (in contrast to links which are temporarily established).

Digital • A means of storing, processing and transmitting information by using distinct electronic or optical pulses that represent the binary digits 0 and 1. Digital transmission and switching technologies use a sequence of these pulses to represent information as opposed to the continuously variable analog signal. The precise digital numbers preclude any distortion (such as graininess or snow in the case of video transmission, or static or other background distortion in the case of audio transmission).

Diverse routing • A telecommunications network configuration in which signals are transmitted simultaneously along two different paths so that if one path is cut or impaired, traffic can continue in the other direction without interrupting service. The Company's networks generally provide diverse routing.

DS-0, DS-1, DS-3 • Standard North American telecommunications industry digital signal formats, which are distinguishable by bit rate (the number of binary digits (0 and 1) transmitted per second). DS-0 service has a bit rate of 64 kilobits per second. DS-1 service has a bit rate of 1.544 megabits per second and DS-3 service has a bit rate of 44.736 megabits per second. A DS-0 can transmit a single uncompressed voice conversation.

Fiber Miles • The number of route miles of fiber optic cable installed (excluding pending installations) along a telecommunications path multiplied by the number of fibers in the cable. See the definition of "route mile" below.

Fiber Optics • Fiber optic technology involves sending laser light pulses across glass strands in order to transmit digital information. Fiber optic cable is the medium of choice for the telecommunications and cable industries. Fiber is immune to electrical interference and environmental factors that affect copper wiring and satellite transmission.

Orlando
1151 N. Keller Rd., 1st Floor
Suite C
Orlando, FL 32810
407.667.0551

Philadelphia
630 Freedom Business Center
Suite 200
King of Prussia, PA 19406
610.382.2000
Wilmington-Newark, DE

Phoenix
2720 E. Camelback Rd.
Suite 205
Phoenix, AZ 85016
602.912.9898

Pittsburgh
2500 Allegheny Center Office Concourse
Pittsburgh, PA 15212
412.316.4824

Portland
851 SW 6th Ave.
Suite 550
Portland, OR 97204-1342
503.220.2895

Providence
275 Promenade St.
Suite 200
Providence, RI 02908
401.621.8300

Sacramento
603 S St
Sacramento, CA 95814
916 447 0824

Salt Lake City
3 Triad Center
345 West North Temple
Suite 160
Salt Lake City, UT 84180
801 972.2332

San Diego
5355 Mira Sorrento Place
Suite 700
San Diego, CA 92121
619.812.0000

San Francisco
One Bush St.
Suite 510
San Francisco, CA 94104
415.276.0000
Oakland
San Jose

Seattle
1215 4th Ave.
Suite 1500
Seattle, WA 98161
206.505.0000
Tacoma
Bellingham

South Florida
1 E. Broward Blvd.
Suite 910
Ft. Lauderdale, FL 33301
954.453.4200
Miami
West Palm Beach-Boca Raton

St. Louis
One City Place Dr.
Suite 200
St. Louis, MO 63141-7065
314.569.1551

Tampa
6015 Benjamin Rd
Suite 306-308
Tampa, FL 33634
813 290.0539

Washington, DC
1331 F St., NW
Suite 200
Washington, DC 20004
202.756.2000

Headquarters – Staten Island
Two Teleport Dr.
Staten Island, NY 10311
718.355.2000

Executive Offices
Princeton Technology Center
429 Ridge Rd.
Dayton, NJ 08810
732.392.2000

National Customer Service Center
7630 S. Chester St.
Suite 300
Englewood, CO 80112
303.749.1700

TCG National Markets – East
25 S. Charles St.
Suite 2000, 20th Floor
Baltimore, MD 21201
410.649.0254

TCG National Markets – West
1000 Town Center
Suite 750
Southfield, MI 48705
248.204.0131

TCG CERFnet, Inc.
9805 Scranton Rd.
San Diego, CA 92121
888.CERFnet (237.3638)
www.cerf.net

Affiliates
Cox Fibernet:
Hampton Roads, VA
757.552.6500
New Orleans, LA
504.734.7345
Oklahoma City, OK
405.600.6333

Atlanta
5060 Avalon Ridge Parkway
Suite 600
Norcross, GA 30071
770.326.7150

Baltimore
25 S. Charles St.
Suite 2000
Baltimore, MD 21201
410.649.0300

Birmingham
2101 6th Ave.
Birmingham, AL 35203
205.326.3465

Boston
10 High St., 2nd Floor
Boston, MA 02110
617.476.4760
Brockton
Lawrence
Worcester

Charlotte
200 S. College St.
Suite 600
Charlotte, NC 28202
704.376.2250

Chattanooga
61 Chestnut St.
Suite 310
Chattanooga, TN 37450
423.756.8500

Chicago
233 South Wacker Dr.
Suite 2100
Chicago, Il 60606
312.705.9800
Gary

Cincinnati
358 Gest St
Cincinnati, OH 45203
513.826.9900

Cleveland
7555 E. Pleasant Valley Rd.
Independence, OH 44131
216.861.5520

Columbus
One Columbus
10 W. Broad St., 4th Floor
Columbus, OH 43215
614.469.4845

Dallas
717 N. Harwood St.
Suite 510
Dallas, TX 75201
972.774.6000
Ft. Worth-Arlington

Denver
2530 S. Parker Rd.
Suite 100
Aurora, CO 80014
303.537.2000
Boulder-Longmont

Detroit
1000 Town Center
Suite 150
Southfield, MI 48075
248.204.0000

Hartford
750 Main St.
Hartford, CT 06103
860.509.9900
New London-Norwich
New Haven-Meriden
Bridgeport
Danbury
Waterbury

Houston
1301 Fannin St
Suite 1290
Houston, TX 77002
713.830.8244

Indianapolis
9325 Delegates Row
Indianapolis, IN 46240
317.532.9900

Knoxville
900 S. Gay St.
Suite 500
Knoxville, TN 37902
423.540.4183

Los Angeles
700 S. Flower St.
Suite 810
Los Angeles, CA 90017
213.787.0000
Orange

Milwaukee
11 E. Kilbourn Ave.
Suite 2100
Milwaukee, WI 53202
414.290.9800
Racine
Kenosha

Minneapolis-St. Paul
511 11th Ave. South
Suite 342
Minneapolis, MN 55415
612.317.4646

Nashville
49 Music Square West
Suite 200
Nashville, TN 37203
615.986.9900

New Jersey
275 Old New Brunswick Rd.
Piscataway, NJ 08854
732.394.4400
Bergen-Passaic
Jersey City
Newark
Trenton-Princeton

New York
One World Trade Center
Suite 5121
New York, NY 10048
212.478.8000
Nassau-Suffolk

Omaha
2505 S. 72nd St.
Omaha, NE 68124
402.384.8000

PRIVATE LINE SERVICES

TCG OmniRing℠ Private Line Services have emerged as the strongest link in the phone chain. These services are offered via TCG's premier fiber optic SONET networks, which connect long distance companies, Incumbent Local Exchange Carrier (ILEC) central offices and corporate end-user buildings at operating standards that surpass those by which today's local carriers are judged.

TCG's unique blend of local presence, centralized support and national coverage means the company can grow its network where customers need it the most. National or local, large or small, corporate or carrier, TCG offers what you need.

TCG OmniRing Private Line Service offerings are calculated on a flat monthly rate, regardless of how much traffic is transmitted. Services include the following:

OmniRing℠ DS0 and DDS (Digital Data Services) • For simple everyday business communications (telephones, fax machines and PC modems), in a variety of voice and data speeds.

OmniRing℠ DS1 • A mid-range service to build corporate "backbone" networks, or link customer locations to long distance carriers or other customer locations. DS1s are used for voice transmissions, as well as LAN interconnection, and accommodate data transmission speeds up to 1.544 mbps (equivalent to 24 voice-grade circuits).

OmniRing℠ DS3 • A high-capacity digital service used by long distance carriers for central office connections and by some large corporate users to link multiple sites. This service permits data transmission at 45 mbps (equivalent to 28 DS1 circuits or 672 voice-grade circuits).

OmniRing℠ SONET Services • A standard Optical Carrier (OC) product for those requiring enhanced network survivability, advanced network architecture and flexible bandwidth utilization. Enjoy the benefit of dedicated, private, local OC3, OC12 or OC48 SONET rings between customer-designated sites and TCG nodes. OC3c, and soon-to-be-released OC12c, support the growing appetite for unchannelized bandwidth at 155 mbps and 622 mbps.

OmniRing℠ E1 (European Standard) • TCG was the first, and in many markets is still the only, provider to offer this service, allowing customers to accommodate their international traffic at 2.048 mbps.

OmniRing LATA Manager • Targeted toward customers who prefer to outsource their local telecommunications networks. TCG takes over the day-to-day management of customers' networks, enabling them to focus their energies on their core business.

INTERNET SERVICES

CERFnet℠ Internet Services • With its CERFnet acquisition, TCG offers a full range of Internet-related services for businesses including dial-up and dedicated Internet access, Web hosting and colocation services and Internet training.

WIRELESS SERVICES

OmniWave℠ • TCG's 38 GHz milliwave private line service supports capacities of: (4) DS1s, (8) DS1s, and (1) DS3. These services can be MUXed at either end to provide lower levels of bandwidth. OmniWave utilizes a broadband milliwave transmission spectrum for quality and reliability that's comparable to conventional fiber networks.

PAYPHONE SERVICES

TCG Payphone Services provide full public pay telephone service to public customers and dial tone services and access lines to other public pay telephone providers.

VIDEO SERVICES

TCG provides analog video link services to its media industry customers, including all of the major television networks as well as to many cable services and independent programmers. The company's video services include offering a broadcast-quality, analog channel which can be provided on a point-to-point or point-to-multipoint basis.

For more information call: 1.800.889.4TCG or contact your local TCG office. Visit us at our web site: **www.tcg.com**

SWITCHED SERVICES

TCG's family of enhanced switched services provides customers with local calling capabilities and connections to their inter-exchange carriers. In most medium- and large-sized corporations today, communications switching, or routing, can most efficiently be handled by subscribing to central office-based switching services and letting the service provider do as much of the work as the customer wants.

PrimeNBX℠ • An excellent alternative to Private Branch Exchange (PBX) switches, which customers must purchase or lease, and then install and maintain. With PrimeNBX, TCG owns, houses and maintains the switch, enabling the customer to avoid unproductive investments in space, capital and personnel. PrimeNBX represents a liberating, future-ready solution that allows customers to focus resources on their business rather than on telecommunications. PrimeNBX relieves the customer of the threat of being locked into obsolete systems when situations such as the recent changes to the North American Numbering Plan occur.

PrimeXpress℠ • Allows customers with their own PBX switches to access TCG's local network and their choice of long distance carrier.

PrimePath℠ • Enables customers to connect to the TCG network using Prime Business Lines or Prime Business PBX Trunks. PrimePath is available in a variety of feature packages which have been developed to serve TCG customers, with features such as Call-Waiting, Call-Forwarding, Conference Calling and PrimeMail℠ voice mail.

PrimeOne℠ • A basic local telephone service product which can be tailored to customers' particular calling requirements. PrimeOne services include Operator and Directory Assistance, as well as an optional regional calling (intraLATA toll) plan. TCG local calling plans can offer significant savings compared to offerings from the incumbent phone company.

PrimePlus℠ • A customized, high quality extended local calling plan available to PrimeNBX and PrimeXpress customers. TCG works with clients to devise cost saving intraLATA (extended area) calling programs based on actual usage and calling needs.

PrimePlex℠ • Provides TCG's customers with multiple voice and data communication services over a single telecommunications line. The company's ISDN services allow customers to perform multiple functions such as simultaneous voice and computer links, and enable TCG to offer customers value-added features.

DATA SERVICES

TCG's award-winning Data Services offer customers a variety of advanced, high-speed data communications options. Customers can choose from a comprehensive family of LAN, MAN and WAN services based on an ATM (Asynchronous Transfer Mode) and SONET (Synchronous Optical Network) backbone. TCG Data Services provide the highest standards in reliability and flexibility, enabling users to reduce operational costs associated with interconnecting various geographically dispersed and architecturally diverse locations.

OmniLAN℠ • Connects workstations and PC users on one or more Local Area Networks (LANs). Users can share files and databases as if they were all working on the same LAN, eliminating delays or "bottlenecks" and allowing data transmissions to take place as fast as the network capacity permits (10 mbps for Ethernet LANs, 4 or 16 mbps for Token Ring LANs, or 100 mbps for FDDI).

OmniStream℠ • Supports both ATM and Frame Relay User-to-Network interfaces (UNIs) and Network-to-Network interfaces (NNIs), offering customers a wide array of options for connecting locally and to all major interexchange carriers. TCG OmniStream services are transported over an ATM/SONET backbone and based on state-of-the-art architecture that automatically formats all services in ATM cells.

SELECTED FINANCIAL DATA

The following table presents historical summary combined financial data for the years 1993, 1994 and 1995, derived from the combined audited historical financial statements of TCG and TCG Partners. The selected consolidated financial data set forth below for the years 1996 and 1997 have been derived from the consolidated financial statements of TCG. The financial statements for the years 1995 through 1997 have been audited by Deloitte & Touche LLP, independent auditors, whose report thereon appears elsewhere in this annual report.

	Years Ended December 31,				
(Dollars In Thousands, Except Per Share Amounts)	**1997**	1996	1995	1994	1993
Statements of Operations Data:					
Revenues:					
Telecommunications services	**$ 494,304**	$ 244,864	$ 134,652	$ 99,983	$ 82,374
Management and royalty fees [1]	**—**	22,805	31,517	20,691	1,555
Total Revenues	**494,304**	267,669	166,169	120,674	83,929
Operating expenses	**283,440**	157,591	93,118	76,572	54,218
Selling, general and administrative [2]	**165,977**	85,025	50,475	39,989	34,281
In-process research and development costs [3]	**22,000**	—	—	—	—
Depreciation and amortization	**155,402**	78,416	37,837	19,933	16,197
Operating loss	**(132,515)**	(53,363)	(15,261)	(15,820)	(20,767)
Other income (expense) net	**(88,488)**	(59,294)	(38,142)	(13,736)	(1,653)
Loss before income taxes	**(221,003)**	(112,657)	(53,403)	(29,556)	(22,420)
Income tax (provision) benefit	**(1,664)**	(2,193)	(401)	(433)	4,149
Net loss	**$ (222,667)**	$ (114,850)	$ (53,804)	$ (29,989)	$ (18,271)
Net loss per share	**$ (1.34)**	$ (1.00)	$ (0.77)	$ (0.43)	$ (0.26)
Weighted average number of shares	**165,728,059**	114,443,695	70,000,140	70,000,140	70,000,140
Other Data:					
EBITDA [4]	**$ 44,887**	$ 25,053	$ 22,576	$ 4,113	$ (4,570)
Cash flows from operating activities	**(21,211)**	93,618	36,141	87,753	47,438
Cash flows from investing activities	**(341,624)**	(913,513)	(207,967)	(265,026)	(149,107)
Cash flows from financing activities	**258,626**	1,085,573	157,688	171,557	129,822
Capital expenditures [5]	**501,035**	308,112	154,807	143,276	155,184
Ratio of earnings to fixed charges [6]	**—**	—	—	—	—
Balance Sheet Data:					
Cash and cash equivalents and marketable securities	**$ 480,159**	$ 718,346	$ 11,862	$ 26,000	$ 31,716
Working capital	**224,889**	545,325	(47,083)	(32,719)	(15,278)
Fixed assets — at cost	**1,873,083**	1,304,229	545,653	422,964	329,686
Total assets	**2,456,301**	2,050,097	614,793	486,983	365,202
Long-term debt (including capital lease obligations)	**1,054,079**	1,021,063	368,464	200,462	29,689
Minority interest	**—**	—	4,409	2,903	12,661
Stockholder's equity and partners' capital (deficit)	**1,031,616**	796,870	125,348	179,152	209,141

[1] Under the terms of various management services arrangements among TCG and its unconsolidated Local Market Partnerships and certain other affiliates, TCG provided operating and administrative support services to such entities, for which it earned management fees. Upon consummation of the TCG Reorganization, these fees were no longer reflected as revenues.

[2] Included in selling, general, and administrative expenses are expenses incurred for services provided to the Local Market Partnerships, in the amounts of $21.4 million, $29.6 million, $19.4 million and $[illegible] 4 million for the years 1996, 1995, 1994 and 1993, respectively.

[3] In December 1997, TCG evaluated the acquired assets and liabilities of CERFnet, and as a result of the evaluation, TCG expensed acquired in-process research and development costs.

[4] EBITDA consists of earnings (loss) before interest, income taxes, depreciation, amortization, minority interest and equity in losses of unconsolidated affiliates. It is a measure commonly used in the telecommunications industry and is presented to assist in understanding TCG's operating results. EBITDA is not intended to represent cash flows or results of operations in accordance with U.S. GAAP for the periods indicated. TCG's use of EBITDA may not be comparable to similarly titled measures due to the use by other companies of different financial statement components in calculating EBITDA. In 1997, this amount represents Recurring EBITDA which is defined as EBITDA excluding a one-time non-recurring charge for acquired in-process research and development costs.

[5] Capital expenditures for 1996 are net of the effect of the inclusion of the Local Market Partnerships as of June 30, 1996.

[6] The ratio of earnings to fixed charges is computed by dividing pre-tax income from operations before fixed charges (other than capitalized interest) by fixed charges. Fixed charges consist of interest charges and the amortization of debt expense and discount or premium related to indebtedness, whether expensed or capitalized, and that portion of rental expense the Company believes to be representative of interest. For the years 1997, 1996, 1995, 1994 and 1993, earnings were insufficient to cover fixed charges by $221.0 million, $116.2 million, $54.1 million, $31.0 million and $23.2 million, respectively.

transaction and/or recover damages and fees in the event that the transaction is consummated. The complaint seeks to have the action certified for class action status and to appoint the plaintiff as the class representative.

Plaintiffs' counsel in the above three putative stockholder class action proceedings have agreed (i) to defer the obligation of the defendants to answer the actions and (ii) to consolidate the actions by filing an amended consolidated complaint. As of the end of February 1998, the amended consolidated complaint had not been filed. The Company believes that these proceedings, individually and in the aggregate, are without merit and that any associated costs will not have a material adverse effect on TCG's financial condition, results of operations or cash flows.

In the ordinary course of business, TCG is involved in various litigation and regulatory matters, proceedings and claims. In the opinion of TCG's management, after consultation with counsel, the outcome of such proceedings will not have a materially adverse effect on TCG's financial position, results of operations or cash flows.

12. Supplemental Disclosure of Cash Flow Information

Cash paid for interest and non-cash investing and financing activities for the years ended December 31, 1997, 1996 and 1995 were as follows (in thousands):

	1997	1996	1995
Cash paid during the year for interest	**$43,008**	$ 7,818	$8,675
Fixed assets acquired under capital leases	**$38,244**	$ 14,034	$ 15,151
Compensation paid in stock	**$ 4,772**	—	—
Rights-of-way obtained in exchange for cable installation	**$ —**	$ —	$ 1,330
Conversion of subordinated debt to parents plus accrued interest	**$ —**	$263,602	$ —
Conversion and stock split of $1 par value common stock to 139,250,370 shares of Class B Common Stock as part of the TCG Reorganization	**$ —**	$ 213,099	$ —
Acquisition of subsidiaries	**$131,246**	$ —	$ —
Cash acquired in acquisitions	**1,203**	—	—
Common stock issued	**123,334**	—	—
	124,537	—	—
Cash paid to acquire subsidiaries	**$ 6,709**	$ —	$ —

13. Selected Quarterly Information (Unaudited)

Summarized below is quarterly financial information for the years ended December 31, 1997 and 1996 (in thousands, except per share amounts):

1997	1st Quarter Consolidated	2nd Quarter Consolidated	3rd Quarter Consolidated	4th Quarter Consolidated	Total
Revenues	**$ 96,844**	**$115,664**	**$ 131,406**	**$150,390**	**$ 494,304**
Net loss	**(45,028)**	**(51,332)**	**(53,784)**	**(72,523)**	**(222,667)**
Loss per common share	**$ (0.28)**	**$ (0.31)**	**$ (0.33)**	**$ (0.42)**	**$ (1.34)**

1996	1st Quarter Combined	2nd Quarter Combined	3rd Quarter Consolidated	4th Quarter Consolidated	Total
Revenues	$ 50,435	$ 57,087	$ 72,749	$ 87,398	$ 267,669
Net loss	(18,693)	(19,743)	(33,705)	(42,709)	(114,850)
Loss per common share	$ (0.25)	$ (0.27)	$ (0.21)	$ (0.27)	$ (1.00)

14. Subsequent Event (Unaudited)

On March 11, 1998, for reasons beyond the control of both parties which made it impossible to conclude the USW Merger prior to the March 31, 1998 termination date, ACC and USW agreed to a mutual termination of the USW Merger Agreement.

Teleport Communications is obligated to pay to the Port Authority 5% of its gross revenues, and may be required to pay a "net return rental fee," as defined, to the extent its cumulative net return exceeds the entitlement amount. For the years ended December 31, 1997, 1996 and 1995 the payments made were $300 thousand in each year. Teleport Communications is required to remit to the Port Authority a minimum payment currently equal to $300 thousand annually.

Teleport Communications entered into a 15-year franchise agreement with the City of New York during 1994, which among other things, requires a payment based on certain gross revenues, as defined in the agreement. The franchise provides for the payment of 10% of certain gross revenues in 1995 and 1996, 6% in 1997 and 5% thereafter, all subject to certain setoffs, reductions and adjustments. The franchise also provides that commencing with calendar year 1995, payment to the City will be no less than $200 thousand per year. For the years ended December 31, 1997, 1996 and 1995 the payments made to the City under the franchise were $1.1 million, $0.8 million and $0.3 million, respectively.

Litigation

In April 1997, a complaint seeking damages in an unspecified amount was filed against the Company in the Circuit Court of Cook County, Illinois by two former customers of the Company and an alleged class purporting to consist of investors in one of the customers, alleging fraud and breach of contract. The initial complaint was dismissed in September 1997 and an amended complaint was refiled by the plaintiffs in October 1997. The Company, upon consultation with counsel, believes that the allegations are without merit and that it possess meritorious counterclaims for damages arising from breach of contract. The Company additionally believes that any costs arising from this lawsuit will not have a material adverse effect on its financial condition, results of operations or cash flows.

On December 16, 1997, prior to public announcement of the AT&T Merger, an action was filed by one TCG public stockholder in the Delaware Court of Chancery against TCG, TCG's directors and the Cable Stockholders. The plaintiff's complaint alleges that, based on public reports, TCG's directors, management and controlling stockholders were negotiating the sale of TCG to AT&T on a preferential basis. This sale on a preferential basis, the complaint alleges, would offer little or no premium over the current market price of TCG Class A Common Stock and is therefore unfair and inadequate to TCG's public stockholders. The plaintiff seeks to enjoin the merger of TCG and AT&T or, alternatively, to rescind the transaction and/or recover damages in the event that the transaction is consummated. The complaint seeks to have the action certified for class action status and to appoint the plaintiff as the class representative.

On January 12, 1998, an action was filed by two TCG public stockholders in the Delaware Court of Chancery against TCG, certain TCG directors and officers, the Cable Stockholders and AT&T. The complaint alleges that the exchange ratio in the AT&T Merger represents an inadequate premium for stockholders of TCG Class A Common Stock. The complaint further alleges that the actions of the TCG directors, officers and Cable Stockholders in connection with the AT&T Merger constitute a breach of various fiduciary duties owed to the stockholders of TCG Class A Common Stock. The plaintiffs seek to enjoin the merger of TCG and AT&T or, alternatively, to rescind the transaction and/or recover damages in the event that the transaction is consummated. The complaint seeks to have the action certified for class action status and to appoint the plaintiffs as the class representatives.

On January 28, 1998, an action was filed by a TCG public stockholder in the Delaware Court of Chancery against TCG, certain TCG directors and officers, and the Cable Stockholders. The complaint alleges that the exchange ratio in the AT&T Merger represents an inadequate premium for stockholders of TCG Class A Common Stock. The complaint further alleges that the actions of the TCG directors, officers and Cable Stockholders in connection with the AT&T Merger constitute a breach of various duties owed to the stockholders of TCG Class A Common Stock. The plaintiffs seek to enjoin the merger of TCG and AT&T or, alternatively, to rescind the by TCG. TCG and Sprint PCS have continued this service relationship throughout 1997. The amount receivable from Sprint PCS at December 31, 1997 and 1996, respectively, was $1.6 million and $0.3 million.

In connection with the management of the Local Market Partnerships, TCG entered into management services agreements. Under the terms of such agreements, TCG provided certain operating and administrative services to such entities, for which it earned management fees. Management fees earned were approximately $0, $21.8 million and $29.6 million in 1997, 1996 and 1995, respectively. After July 2, 1996, such management fee revenue is no longer recorded because the previously unconsolidated partnerships are now consolidated.

Related to the acquisition of KCFN, TCG is liable to fund the operations until the closing. Such liability for KCFN as of December 31, 1997 is $2.3 million which is included in accounts payable and accrued liabilities. The liability associated with the acquisition of KCFN of approximately $55 million is included in accounts payable and accrued liabilities.

11. Commitments and Contingencies

Operating Leases

Under the terms of contracts with various parties, TCG is obligated to pay franchise fees, office rents, node rents and rights-of-way fees in connection with its fiber optic network through 2022. These contracts provide for certain scheduled increases and for possible escalation of basic rentals based on a change in the cost of living or on other factors. TCG expects to enter into other contracts for additional franchise fees, office rents, node rents, rights-of-way facilities, equipment, and maintenance services in the future.

A summary of such fixed commitments at December 31, 1997 is as follows (in thousands):

Years	Amount
1998	$ 34,079
1999	32,286
2000	29,986
2001	27,908
2002	25,723
Thereafter	65,814
Total	$215,796

Rent expense under operating leases was approximately $31.4 million, $18.0 million and $11.8 million for the years ended December 31, 1997, 1996 and 1995, respectively.

Capital Leases

Communications network includes assets acquired under capital leases of approximately $154.1 million and $114.1 million (including approximately $111.6 million and $96.0 million with related parties) at December 31, 1997, and 1996, respectively. The related accumulated depreciation and amortization was approximately $18.9 million and $12.1 million, respectively.

The following is a schedule, by year, of future minimum payments under the leases, together with the present value of the net minimum payments as of December 31, 1997 (in thousands):

Years	Amount
1998	$38,218
1999	12,545
2000	4,860
2001	844
2002	534
Thereafter	4,130
Total minimum lease payments	61,131
Less amount representing interest	8,312
Total obligations under capital leases	$52,819

Retention Incentive

As part of the AT&T Merger, TCG has offered a retention incentive compensation package to all employees as of January 8, 1998. These amounts are payable in four installments, the closing date of the proposed AT&T Merger, the first anniversary of the closing date, the second anniversary of the closing date and thereafter to all employees still employed at TCG. Such amounts are currently estimated at $14.4 million, $14.4 million, $10.4 million and $0.8 million, respectively. There are no assurances that the AT&T Merger will be consummated.

Revenue Sharing Agreements

Teleport Communications is subject to a revenue sharing agreement with The Port Authority of New York and New Jersey (the "Port Authority"). Based on the agreement, temporary differences compose the net deferred income tax payable (in thousands):

	1997	1996
Deferred income tax liabilities:		
Depreciation, amortization and excess credits	**$ 73,868**	$ 43,072
Other	**553**	—
	74,421	43,072
Deferred income tax assets:		
Operating loss	**(192,433)**	(81,578)
Deferred revenue	**(2,403)**	(2,361)
Assets recorded for tax purposes	**(3,575)**	(3,368)
Incentive compensation	**(6,434)**	(4,579)
Equity in losses of unconsolidated subsidiaries	**(142)**	(138)
Other	**(248)**	—
	(205,235)	(92,024)
Less: valuation allowance	**131,778**	49,874
Total deferred tax assets	**(73,457)**	(42,150)
Deferred income taxes payable — net	**$ 964**	$ 922

In 1997, 1996 and 1995, the net income tax benefits of approximately $81.9 million, $29.6 million and $10.9 million, respectively, have been offset by increases in the valuation allowance of $81.9 million, $29.6 million and $10.9 million, respectively, due to the uncertainty of realizing the benefit of the loss carry-forwards.

At December 31, 1997, TCG had operating loss carry-forwards for federal income tax purposes of approximately $523.0 million, expiring principally in 2003 through 2013. Approximately $49.0 million of the net operating loss carry-forwards are carryovers related to the acquisitions of BizTel and ETC. The net operating losses related to these acquisitions will be subject to various limitations.

A reconciliation of the statutory federal income tax rate and TCG's effective income tax rate is as follows:

	1997	1996	1995
Statutory federal income tax rate	**35.00%**	35.00%	35.00%
State and local taxes, less federal benefit	**0.75**	2.36	1.30
Unutilized tax benefit due to net operating loss	**(30.04)**	(31.80)	(33.30)
Permanent differences and other	**(4.96)**	(3.20)	(1.70)
Effective rate	**0.75%**	2.36%	1.30%

10. Related Party Transactions

In 1996 TCG entered into a preliminary agreement with TCI which provided for the provision of certain services by TCG to TCI in connection with the development by TCI of residential telephony service offerings in Hartford, Connecticut, Fremont, California and Arlington Heights, Illinois and possibly other locations. TCI has agreed to reimburse TCG for certain costs and cost of capital in connection with these services. TCG is also in the process of negotiating a market based agreement for the provision of telephony services for TCI in multiple dwelling units at various locations. TCI and TCG are continuing negotiations to reach a definitive agreement for both offerings. At December 31, 1997 and 1996, the amounts due to TCG for this reimbursement were $1.0 million and $1.1 million, respectively, and are included in accounts receivable-related parties. TCG has entered into an agreement with Comcast to support a Comcast residential service offering to be conducted in Maryland and Florida.

TCG also provides management services to certain affiliates of Cox under three Operator Managed Ventures Services Agreements, including billing services, network monitoring and accounts receivable functions. Under the terms of the agreements, TCG retains 8% of the collected revenues from Cox customers as a royalty fee. Royalty fees recorded from Cox were approximately $0.6 million, $0.3 million and $0.1 million for the years ended December 31, 1997, 1996 and 1995, respectively. Included in accounts receivable — trade are approximately $1.0 million and $0.4 million at December 31, 1997 and 1996, respectively, for amounts owed by Cox customers. At December 31, 1997 and 1996, the amounts due to Cox affiliates under the agreements were $1.7 million and $1.1 million, respectively.

In 1997 and 1996, TCG purchased cable on behalf of certain of the Cable Stockholders, which it then sold to them at cost. The amount receivable from the owners was $1.1 million and $1.5 million as of December 31, 1997 and 1996, respectively.

Sprint PCS, a partnership owned 60% by TCI, Comcast and Cox, entered into service agreements or letters of intent with a number of wholly-owned subsidiaries of TCG providing for the construction of special facilities and the provision of services to Sprint PCS

Valuation Assumptions — The fair value of options at the date of grant was established using the Black-Scholes model with the following weighted average input assumptions:

	Expected Life	Exercise Price	Stock Price at Grant	Volatility	Risk Free Int. Rate	Div. Yield	Annual Forfeiture Rate
1996 Employee Stock Purchase Plan Grants	1.00	$ 13.60	$ 16.00	25.0%	5.81%	0%	4.89%
1995, 1996 and 1997 Stock Option Grants	5.00 to 7.00	$ 14.22 to $46.98	$ 14.22 to $46.98	0.1% to 26.4%	5.80% to 6.73%	0%	0% to 5.00%

The following table summarizes information concerning the remaining options outstanding as of December 31, 1997 for the 1997, 1996 and 1995 option grants and the 1997 Employee Stock Purchase Plan:

	Options Outstanding				Options Exercisable	
	Range of Exercise Prices	Number of Shares Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Prices	Number of Shares Exercisable	Weighted Average Exercise Prices
1995, 1996 and 1997 Stock Option Grants and 1997 Employee Stock Purchase Plan	$ 14.22 to $55.02	4,011,154	5.00 to 7.00	$ 14.22 to $46.98	2,313	$14.22

Employment Agreements — TCG has employment agreements with certain of its executive officers and senior management personnel. These agreements are effective through dates ending from June 30, 1998 to December 31, 2000, unless terminated earlier by the executive or TCG, and provide for annual salaries, cost-of-living adjustments, additional compensation in the form of bonuses based on the performance of TCG and the executive, and participation in the various benefit plans of TCG. The agreements contain certain benefits to the executive if TCG terminates the executive's employment without cause or if the executive terminates his employment as a result of change in ownership of TCG. The salary and bonus expense related to these employment agreements for the years ended December 31, 1997, 1996 and 1995 approximated $3.6 million, $2.9 million and $2.1 million, respectively. TCG's remaining aggregate commitments for salaries under such agreements is approximately $4.9 million. The commitments for bonuses under these agreements is approximately $1.9 million.

In the event TCG terminates the executive without cause or the executive terminates his/her employment as a result of a change in control, the agreements provide for continued vesting in deferred compensation and long term incentive awards as well as the payment of a base salary for each executive plus an annual bonus for the duration of the agreement. The annual bonus is an amount not less than 30% of such base salary, except for a certain employee whose minimum annual bonus is 50% of base salary. Each executive is entitled to these severance benefits for at least six months following such termination, except for a certain employee whose minimum entitlement period is 30 months.

9. Income Taxes

There are no current income taxes payable based on TCG's operating loss. The current state and local tax expense are based on factors other than income. The following the 1997 Stock Purchase Plan. The expense recorded for the year ended December 31, 1997 related to options issued was approximately $0.3 million.

Teleport Communications Group Inc. Employee Stock Purchase Plan (1996) — TCG adopted the Teleport Communications Group Inc. Employee Stock Purchase Plan (the "1996 Stock Purchase Plan"), effective June 27, 1996. The 1996 Stock Purchase Plan is administered by the Committee. Each eligible employee was given an option to purchase a number of shares of Class A Common Stock up to 10% of such employee's compensation plus bonus paid for the calendar year preceding the year the option is awarded, divided by the purchase price per share under the option. No employee can receive options for more than $25 thousand worth of shares in any calendar year. The purchase price for one share of Class A Common Stock is 15% below the initial offering price of $16, or $13.60. The Board of Directors has authorized the issuance of 745,000 shares under the 1996 Stock Purchase Plan. The options expired on June 27, 1997. Options related to 584,686 shares of Class A Common Stock were exercised.

The expense recorded in each of the years ended December 31, 1997 and 1996 related to the options issued was approximately $0.7 million.

The following table provides additional information concerning the 1996 and 1997 Employee Stock Purchase Plans

	Shares of Common Stock		
	Available for Grant	Outstanding	Exercise Price
Balance, January 1, 1996	—	—	$ —
Authorized	745,000	—	13.60
Granted	(623,894)	623,894	13.60
Exercised	—	—	—
Forfeited	41,001	(41,001)	13.60
Balance, December 31, 1996	162,107	582,893	$ 13.60
Authorized	1,500,000	—	—
Granted	(109,975)	109,975	35.54
Exercised	—	(609,651)	13.60–35.54
Forfeited	83,217	(83,217)	13.60
Balance, December 31, 1997	**1,635,349**	—	$ —

Stock-Based Compensation — In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation," which encourages but does not require companies to record compensation cost for stock-based compensation plans at fair value.

TCG has chosen to continue to account for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion ("APB") No. 25 "Accounting for Stock Issued to Employees," and its related interpretations. Accordingly, no compensation expense has been recorded for its stock awards and employee stock purchase plans, but rather, the Company has determined the pro forma net loss and net loss per share amounts for 1997, 1996 and 1995, as if compensation expense had been recorded for options granted during those years under the fair value method described in SFAS No. 123. Compensation cost for stock options is measured as the excess, if any, of the quoted market price of the Company's stock at the date of the grant over the amount an employee must pay to acquire the stock. Compensation cost for stock appreciation rights and performance equity units is recorded quarterly based on the quoted market price of TCG's stock at the end of the period.

The Company utilized the Black-Scholes option pricing model to estimate the fair value at the date of grant of options granted during 1997, 1996 and 1995. Under the Black-Scholes model, the volatility factor ranged from 25.0% to 26.4% was used for options granted on or after the date of the 1996 Offerings and the minimum value method was used for options granted prior to the date of the 1996 Offerings, as if there was no market for the Company's common stock in which to monitor stock price volatility. Had TCG adopted SFAS No. 123, net loss and loss per share would have increased as indicated below (in thousands, except share amounts):

	1997	1996	1995
Net loss — as reported	**$(222,667)**	$(114,850)	$(53,804)
Net loss — pro forma	**$(225,625)**	$(116,398)	$(53,929)
Loss per share — as reported	**$ (1.34)**	$ (1.00)	$ (0.77)
Loss per share — pro forma	**$ (1.36)**	$ (1.02)	$ (0.77)
Weighted average number of shares outstanding	**165,728,059**	114,443,695	70,000,140

shares in the event of death, total disability or a change in control. In the event a participant's employment is terminated for cause, his/her interest in each and every share awarded under the Equity Incentive Plan shall be forfeited.

Shares under the Equity Incentive Plan will be paid to a participant either in one lump sum cash payment or in shares of Class A Common Stock, as determined at the discretion of the Compensation Committee, on the payment date elected by the participant at the time he/she elects to participate in the Equity Incentive Plan. In general, the payment date elected may be the last business day of any calendar quarter during the period commencing June 30, 1998 and ending June 30, 2001.

At December 31, 1997 and 1996, respectively, 409,983 and 421,233 shares were outstanding under the Equity Incentive Plan.

Teleport Communications Group Inc. Stock Option Plan — TCG established the Teleport Communications Group Stock Option Plan (the "SOP") effective September 26, 1993. The SOP is administered at the discretion of the Compensation Committee, which has made long-term incentive compensation awards in the form of non-qualified and incentive stock options to eligible employees. Stock options were granted with exercise prices at or above the fair market value of the shares on the date of grant, and no compensation expense has been recognized in connection with the options. The Compensation Committee may permit the exercise price to be paid in cash, through delivery of other shares of Class A Common Stock, by delivering irrevocable instructions to a financial institution to deliver promptly to TCG the portion of sale or loan proceeds sufficient to pay the exercise price, or through an election to have shares withheld from the shares otherwise to be received by the option holder.

The following table provides additional information concerning the SOP:

	Shares of Common Stock		
	Available for Grant	Outstanding	Exercise Price
Balance, January 1, 1995	2,888,046	2,495,304	$ 6.90—10.39
Authorized	—	—	—
Granted	(285,096)	285,096	14.22
Exercised	—	(27,115)	6.90
Forfeited	215,225	(215,225)	6.90—14.22
Balance, December 31, 1995	2,818,175	2,538,060	$ 6.90—14.22
Authorized	5,547,683	—	—
Granted	(2,003,462)	2,003,462	17.46—21.60
Exercised	—	(55,355)	6.90
Forfeited	173,443	(173,443)	6.90—21.60
Balance, December 31, 1996	6,535,839	4,312,724	$ 6.90—21.60
Authorized	**—**	**—**	**—**
Granted	**(1,935,068)**	**1,935,068**	**24.48—55.02**
Exercised	**—**	**(285,332)**	**6.90—10.39**
Forfeited	**155,944**	**(155,944)**	**6.90—49.00**
Balance, December 31, 1997	**4,756,715**	**5,806,516**	**$ 6.90—55.02**

Teleport Communications Group Inc. Employee Stock Purchase Plan (1997) — TCG adopted the Teleport Communications Group Inc. Employee Stock Purchase Plan (the "1997 Stock Purchase Plan"), effective July 1, 1997. The 1997 Stock Purchase Plan is administered by the Compensation Committee of the Board of Directors (the "Committee"). As of the first day of each calendar quarter each eligible employee will be granted the option to purchase as of the last day of each calendar quarter, a number of shares determined under a uniform formula specified by the Committee. Each eligible employee was given an option to purchase the number of shares equal to 10% of such employee's compensation plus bonus paid in that calendar quarter, divided by the purchase price per share under the option. No employee can receive options for more than $25 thousand worth of shares in any calendar year. The purchase price for one share of Class A Common Stock is 15% below the average closing price of the last ten trading days of the calendar quarter. The Committee authorized the issuance of 1,500,000 shares of Class A Common Stock under respectively. Each Unit is equal to 8.4 shares of Class A Common Stock. Except for awards to a certain employee, the appreciation of any Unit is limited to 200% of the initial base price. Pursuant to an employee's employment agreement, there is no limit on the appreciation he may receive under the 1992 UAPs. Awards under the UAP are subject to a five-year vesting schedule, pursuant to which the Units granted were 60% vested as of December 31, 1995 and December 31, 1994, respectively, and fully vested no later than December 31, 1997 and December 31, 1996, respectively, subject to certain exceptions provided therein. The 1992 UAPs were fully vested December 31, 1996 and were paid early in 1997. In connection with the UAP, TCG recognized compensation expense of $15 thousand, $1.4 million and $2.5 million for the years ended December 31, 1997, 1996 and 1995, respectively. In January 1996, TCG adopted a plan which permits the awards under the UAP to be deferred in whole or in part at the election of the participants for periods of up to five years or, with the Administrative Committee's consent, until termination of employment.

The following table provides additional information concerning the Unit Appreciation Plan awards:

Year of Award	Initial Number of Units	**Number of Units Outstanding at December 31, 1997**	**Number of Units Vested at December 31, 1997**	**Value of Units Vested at December 31, 1997**	Number of Units Outstanding at December 31, 1996	Number of Units Vested at December 31, 1996	Value of Units Vested at December 31, 1996	Number of Units Outstanding at December 31, 1995
1993	36,000	**5,300**	**5,300**	**$369,410**	5,300	4,240	$ 295,528	23,700
1992	170,850	**—**	**—**	**—**	63,250	63,250	7,695,373	139,200
Total	206,850	**5,300**	**5,300**	**$369,410**	68,550	67,490	$7,990,901	162,900

Teleport Communications Group Inc. 1996 Equity Incentive Plan—TCG established the Teleport Communications Group Inc. 1996 Equity Incentive Plan (the "Equity Incentive Plan") effective June 27, 1996, to provide opportunities for certain employees of TCG to participate in the appreciation in the value of TCG after the initial public offering. The Board of Directors authorized the issuance of up to 637,792 shares of Class A Common Stock under the Equity Incentive Plan. The Equity Incentive Plan is administered by the Compensation Committee which has full and discretionary power to award shares under the Equity Incentive Plan.

Under the Equity Incentive Plan, each employee who had an award under the 1992 UAP or the 1993 UAP, whether or not the employee had elected to defer receipt of the payment of benefits thereunder and who is employed by TCG as of June 27, 1996, had the right to waive his/her interest in all or any portion of the employee's benefit in the 1992 UAP or the 1993 UAP. In exchange therefore, the employee was granted a number of shares under the Equity Incentive Plan equal to the value of the portion of the employee's benefit waived (determined as of June 27, 1996) multiplied by 120% and divided by the initial public offering price per share of Class A Common Stock. No employee could receive more than 54,000 shares under the Equity Incentive Plan, and a certain employee was not eligible to participate. One share under the Equity Incentive Plan is equivalent in value to one share of Class A Common Stock. Thus, the value of the benefit payable under the Equity Incentive Plan will fluctuate in accordance with the fair market value of the Class A Common Stock.

Shares under the Equity Incentive Plan granted in exchange for 1992 UAP benefits are subject to a two-year vesting schedule, with 70% of the shares becoming vested as of June 27, 1997 and the remaining 30% becoming vested as of the June 27, 1998. Shares granted in exchange for the 1993 UAP benefits are subject to a three-year vesting schedule, with 70% of the shares becoming vested as of June 27, 1998 and the remaining 30% becoming vested as of June 27, 1999. A participant shall become 100% vested in his/her